No. 9902

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

GOLDEN STATE THEATRE & REALTY CORPORATION (a California corporation),
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S REPLY BRIEF.

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After a careful examination of respondent's brief filed herein, it is apparent that no attempt has been made to answer the two main points raised by petitioner in this case, viz., first, that treasury stock is of no value, as held by the case of *Borg v. International Silver Co.* (1925), 11 F. (2d) 147 (Pet.'s Opening Brief, p. 9), and, second, that the laws of the State of California are applicable in the determination of whether or not the stock transaction from which this case arose resulted in a taxable gain to petitioner. (See *Blair v. Commissioner* (1937), 300 U. S. 5, 57 S. Ct. 330, Pet.'s Opening Brief, pp. 12, 13 and 14.)

The cases as cited by respondent, commencing with page 6 of his brief, are all distinguishable and, peti-

tioner believes, not pertinent to the two main points involved. Particular attention is called to the fact that considerable reliance is evidently put upon the case of *Commissioner v. S. A. Woods Machinery Co.* (Resp.'s Brief, p. 6), the facts of which involved a situation where the taxpayer accepted shares of its own stock in satisfaction of a judgment obtained against another corporation. It is obvious, of course, that the facts of that case are in no way comparable with the facts of the case before the Court. In the first place, the S. A. Woods Machinery Co. acquired something it did not have before, to-wit, a judgment obtained in the course of its business and satisfied by the acceptance of its own stock. In the second place, consideration of a statute similar to that of the State of California in this case, was not before the Court. It is to be noted that on page 636 of the opinion the Court stated that the debtor corporation might have paid the taxpayer in cash. It then said:

> "If that had been done, clearly the cash received would have been taxable income. The transaction was not changed in its *essential character* by the fact that, as the debtor happened also to own the stock, the money payment and the purchase of stock were by-passed and the stock was directly transferred in payment of the debt. The stock was the medium in which the *debt* was paid."

Again later, the Court stated:

> "Whether the acquisition or sale by a corporation of shares of its own capital stock gives rise to a capital gain or deductible loss *depends upon the real nature of the transaction involved* (citing cases) * * * but where the transaction is not of

> that character and a corporation has legally dealt in its own stock as it might in the shares of another corporation and in so doing has made a gain or suffered a loss, we perceive no sufficient reason why the gain or loss should not be taken into account in computing the total income."

It is obvious from the citation just given that the Court considered this case upon its own peculiar facts and the opinion, therefore, is not necessarily of controlling value in the present case.

It is very clear in the instant case that petitioner was not dealing with its own stock as it would the stock of another corporation nor did it acquire anything that could have been of any value to it under California law.

In none of the other cases cited by respondent did the Court consider any statute similar to that of California.

Respondent insists upon emphasizing that there is no difference between the delivery to petitioner of cash or stock. Under the statutes of the State of California, which are here submitted to the Court to be construed for the first time in this regard, there is a very obvious and important distinction. Money paid to petitioner could have been used by petitioner; goods delivered to petitioner could have been used by petitioner. But its own stock could not be utilized by it for any purpose whatsoever nor could it even be considered as an asset upon its receipt. It has and had no value. (Civil Code of the State of California, Sec. 342b; Pet.'s Opening Brief, pp. 8 and 9; *Borg v. International Silver Co.,*

supra.) Even respondent admits that it is better accounting practice not to treat treasury stock as an asset. (Resp.'s Brief, p. 6.) If it were re-sold, the capital asset represented by the proceeds from the sale immediately becomes offset by a corresponding capital stock liability, and there is no net gain or loss to the corporation.

The respondent, on page 9 of his brief, suggests the possibility of evasion by the taxpayer. While it is felt that the point is of no value at all in determining the issues involved, it may be important to note that no such question should have been raised in this case for the reason that the stock involved was purchased by San Francisco Wigwam Theatre Co., a subsidiary, in 1931 (Tr. pp. 31 to 34 incl.), at which time intercorporate dividends were not taxable. (Revenue Act of 1928, Sec. 23 (p.) (1).) Actually, therefore, if the transfer of the stock from the subsidiary to the parent could be construed, in law or in fact, as a dividend payment, such payment was made in 1931 and not in 1936, and no question of evasion could possibly arise with respect to the transaction. As a matter of fact, the only transaction which really involved property of value was the transaction which occurred in 1931, when the San Francisco Wigwam Theatre Co. purchased the stock involved from outside parties. (Pet.'s Opening Brief, p. 4.) The things done in 1936 were simply bookkeeping entries and did not amount, in any sense of the word, to transfers of property for value or, strictly speaking, were they transactions in relation to the stock at all.

As stated in many of the authorities cited by petitioner and respondent, each case should be determined upon its own facts, and upon its own facts it is contended that this is a situation where no gain resulted and no tax is due.

It is therefore respectfully submitted that the Board of Tax Appeals erred in its decision and that the decision of said Board be reversed.

Dated, San Francisco,
January 16, 1942.

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